

Law Offices Of  
**MORRIS L. SILVER, ESQ.**  
THE KELLOGG FARM  
Stage Road  
Post Office Box 606  
Benson, Vermont 05731-0606  
TELEPHONE 802-537-2264  
FAX 802-537-2265  
MLSILVER@SOVER.NET

December 8, 2006

Ms. Susan M. Hudson, Clerk  
Vermont Public Service Board  
Chittenden Bank Building, Fourth Floor  
112 State Street, Drawer 20  
Montpelier, Vermont 05620

*Via Electronic Mail*

Re: Next Steps on Financing the EEU Budget

Dear Ms. Hudson:

At the close of the Workshops convened by the Public Service Board (the “Board” or “PSB”) to consider the role that a financing tool might play in the delivery of Demand Side Management (“DSM”), the Board advised participants that it would afford them an additional opportunity to provide comments and responses to outstanding information requests. This letter will serve as Central Vermont Public Service Corporation’s (“Central Vermont” or “CVPS”) closing comments and provide a response to the questions asked by the Board concerning the viability of DSM financings issued in amounts less than \$100 million within financial markets. Also appended to this letter is a draft proposal on how a DSM financing mechanism might be structured to create a securitization tool for future use by the Board to finance DSM investments as described during the Board’s workshops. This draft is offered for discussion purposes without prejudice and to help better illuminate issues attendant to the review of DSM financing options.

As a preface to this submission, Central Vermont reiterates the circumstances identified by participants where financing all or part of the EEU budget could be advantageous:

- When “lumpy” investments in DSM are called for to help cost-effectively defer or avoid otherwise required distribution, transmission or generation investments.
- When financing all or some program expenditures would help to mitigate inter-generational inequities by spreading the cost of the DSM measures over their useful life.
- When financing the accelerated acquisition of DSM measures would help

to mitigate potential rate shock, that might occur when the initial DSM costs exceed initial avoided cost benefits.

- Financing could be used in conjunction with a shift from all customers pay program designs to ones where the measure recipient pays (*i.e.*, financing could be used to let customers who receive efficiency measures pay back the loan out of savings over time).
- Financing can help to overcome access to capital barriers for utilities and customers when the acquisition of additional DSM is a sound part of a resource portfolio.

Participants also recognized that financing DSM can have potential disadvantages including:

- Using financing adds debt service costs to the cost of the measures and thereby increases the measure costs at least in a nominal dollar sense. However, debt service will not necessarily increase the economic present value of the costs (although equity financing will because of tax gross-up issues).
- The ability to finance expenditures and defer payments into the future might induce expenditures that would not be undertaken if the financial consequences were immediately realized.
- Depending on the design of the financing strategy, the credit quality of the affected utility or the State could be adversely affected (*e.g.*, increasing the un-collateralized debt of the utility, or reducing the borrowing capacity of the issuer).

Within this context, it generally appeared that the development of a financing tool would be useful in the planning, management and implementation of DSM investments as a part of the provision of “least-cost” service to Vermont electricity consumers.

A. DSM Financings of Less than \$100 million.

At the workshops, the Board asked participants to provide information on whether it would likely be possible to issue DSM financings in face amounts of less than \$100 million. The Board explained that this assumption was based on discussions with VEPP Inc., the Board’s Rule 4.100 Purchasing Agent, concerning the possibility of issuing securitization “mitigation bonds” to buy down qualifying facility contracts under 30 V.S.A. § 209a. Based on a preliminary review conducted by CVPS, it does not appear that the \$100 million assumption is

appropriate for use when considering the potential to use financings to support DSM investments. Central Vermont must caution that much of its research was conducted in connection with the efforts to enact Section 209a and that a securitization financing using this approach has yet to be implemented in Vermont.

Central Vermont's experience with traditional corporate finance has been that the size of a debt issue generally depends on the type of security, the market and the investors' needs. The investment banker working on the issuance, and its contacts, very much influence what can get done. For example, in the 1980s, VIDA (now VEDA) did individual issues for CVPS in the amount of \$5 to \$6 million each in the public market. In 2004, CVPS successfully issued \$75 million of First Mortgage Bonds to private investors who took individual positions of \$5, \$10 or \$15 million.

It should be noted that there are different markets for securities, and the cost and regulatory issues can vary. Moreover, some markets do prefer larger minimum issuances for efficient pricing. Until the specifics of a particular financing proposal are known, however, it is difficult to assess these costs and issues. That said, the Company's basic conclusion is that issuance of financings in amounts much smaller than \$100 million should be possible to support Vermont DSM investments.

B. Structure for DSM Financings.

At the workshops, Central Vermont described a securitization model for consideration as a structure for DSM financings. As detailed by CVPS, such structure would include the following components:

- Upon application by the Department of Public Service, the Energy Efficiency Utility ("EEU") or a Distribution Utility ("DU"), the PSB would be authorized to issue a "qualified DSM financing charge order" to finance the costs associated with development, implementation and monitoring of one or more DSM program as authorized by the Board. Such an order to be issued only following a Board hearing.
- A "qualified DSM financing charge order" would impose "DSM financing charges" payable to the issuer of the "DSM financing bonds."
- A "qualified DSM financing charge order" would contain/establish:
  - (1) a finding that the issuance of such an order will promote the general good;
  - (2) a separately stated non bypassable "DSM financing charge" for the

benefit of the issuer that is payable regardless of any change in structure, identity or ownership of the DU or EEU;

- (3) a specific mechanism for automatic adjustment of the charge, at least annually, so that the charge provides revenues sufficient to make timely payments of accrued interest and scheduled principal on the DSM financing bonds, as well as ongoing administrative expenses, credit enhancement fees and scheduled over-collateralization amounts; and
  - (4) the pledge of the State of Vermont, for the benefit of the issuer and the owners of DSM financing bonds, that neither the charge nor the adjustment mechanism will be altered absent adequate provision for the protection of the issuer.
- “DSM financing charges,” and the right to receive financing charges, would be the property of the issuer and would constitute a present interest in property.
  - DUs would be required to collect DSM financing charges for the benefit of the issuer and remit them to the issuer or its designee. DUs in possession of financing charges would have no right, title or interest in such collections.
  - A “qualified DSM financing charge order” would remain in full force and effect, notwithstanding any bankruptcy of the DU or the EEU.
  - The issuer would be permitted to grant a security interest in, or otherwise assign, DSM financing charges and the right to receive financing charges in connection with the issuance of DSM financing bonds.
  - To attempt to seek tax exempt financing, Vermont could consider creating a Vermont DSM Financing Authority. The purpose of the authority would be to issue financing bonds to pay the costs of DSM that has been approved by the Board in a qualified DSM financing charge order.
  - No bond issued by the Authority would be authorized to obligate the State of Vermont to raise any money by taxation.
  - DSM financing bonds would not be deemed to constitute a general obligation debt or a general liability of the state.

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- DSM financing bonds issued by the authority, and the income there from, could be designed (perhaps in part) to be exempt from taxation by the State of Vermont and its political subdivisions, agencies or instrumentalities.

This structure is designed to protect the interests of stakeholders, including utilities and the state, while helping to grant the Board authority to finance DSM, when such actions are found to be appropriate. To better understand this structure, a draft is attached that attempts to propose specific terms and conditions for consideration by the Board and participants. This draft is offered for discussion purposes and is largely based on Section 209a. Central Vermont hopes that this draft will be helpful and that it can be used to further review and discussion on the desirability of developing a DSM financing tool.

Central Vermont very much appreciates the opportunity to participate in this effort and hopes that this filing will provide useful information for further dialogue and consideration. Should you have questions concerning this submission, please do not hesitate to contact me.

Respectfully submitted,

/s/

Morris L. Silver

MLS/m  
cc: Electronic Service List